



STATE OF CALIFORNIA

STATE BOARD OF EQUALIZATION

450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0086
916-327-8988 • FAX 916-324-2586
www.boe.ca.gov

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February 8, 2008

Mr. William H. Weissman
Littler Mendelson, PC
650 California Street 20th Floor
San Francisco, CA 94108

Dear Mr. Weissman:

Your December 3, 2007 article “*Why Is Buying Hot Chocolate So Confusing?*” was referred to me for response since the Board of Equalization (Board) administers the Sales and Use Tax Law. In your article, you expressed concern regarding the proper application of the sales tax by various retailers with respect to sales of hot chocolate.

According to your article, you purchased a hot chocolate from a Starbucks located inside a Target Store in your hometown of Walnut Creek and were charged sales tax on the purchase price. However, you are not charged sales tax when you purchase a hot chocolate at a Starbucks located within a Safeway in Walnut Creek nor the Starbucks in the lobby of the Bank of America building in downtown San Francisco. You expressed concern that the application of sales tax is unexplainably inconsistent.

For your general information, the California Sales and Use Tax Law imposes a sales tax upon retailers for the privilege of selling tangible personal property at retail in the State of California. The use tax is complementary (and mutually exclusive) to the sales tax and is imposed upon the consumer for the storage, use, or other consumption of tangible personal property in the State of California. Either the sales or the use tax applies to all retail sales of tangible personal property to customers in California, unless otherwise exempted by statute or type of transaction. When use tax is applicable, the consumer is liable for the tax. When sales tax is applicable, the retailer (seller) is liable for the tax. The rate for both taxes is the same.

Sales and Use Tax Regulation 1602, *Food Products*, (copy enclosed), provides that generally tax does not apply to sales of food products for human consumption except as provided in Regulation 1503, 1574 and 1603. “Food products” include among other items, coffee, tea, noncarbonated and nonalcoholic beverages, breads, bakery products, pizzas, candy, confectionery, chewing gum and cookies. Generally, tax does not apply to sales of the above items except when they are sold under circumstances as provided in Regulations 1503, 1574 and 1603.



Sales and Use Tax Regulation 1603, *Taxable Sales of Food Products*, (copy enclosed), provides certain circumstances whereby the sale of food products are taxable. Tax applies to sales of food products when any one of the following situations applies:

- (1) Sales of hot prepared food products with the exception of coffee, hot tea, lattes, mochas, hot chocolate and hot bakery goods when sold “to go” and for a separate price. A food product is considered a hot food product if it is heated to a temperature above room temperature. Hot food is considered taxable even if it has cooled by the time of sale since it was intended to be sold as a hot food.
- (2) Sales of meals or hot prepared food products furnished by a restaurant, concessionaire, hotel, soda fountain or similar establishment.
- (3) Food products furnished, prepared, or served for consumption where facilities are provided by the retailer (tables, chairs, or counters or from trays, glasses, dishes or other tableware).
- (4) Sales of food products by a “drive-in” (food products ordinarily sold for immediate consumption at or near a location where parking facilities are provided primarily for the use of patrons in consuming the products, even though they may sold “to go”).
- (5) Sales of food products within a place where attendants are charged for admission, e.g. theaters, amusement parks, etc.
- (6) Sales of food products by a deli, bakery, cafeteria, restaurant or similar establishment on a “to go” basis, but furnished in a form suitable for consumption on the seller’s premises, when:
 - A) more than 80 percent of the seller’s gross receipts are from the sale of food products, and
 - B) more than 80 percent of the seller’s retail sales of food products are taxable as provided in 1, 2, 3, or 4 above.

To determine whether the seller’s transactions meet the 80-80 Rule criteria, the seller’s operations should be monitored and reviewed for two consecutive calendar quarters. The procedure is explained in Chapter 6 of Publication 22, *Tax Tips for the Dining and Beverage Industry*, (copy enclosed) .

When a seller comes under the 80/80 rule (#6 above), all of his/her food and beverage sales are subject to tax unless he/she makes the special election. To make the election not to report tax on “to go” sales of cold food products, hot beverages, and hot bakery goods the seller must maintain separate accounting and documentation in his or her records. Tax will remain applicable to the sale of food products as provided in 1 through 4 above.

When a seller does not meet both criteria of the 80/80 rule, tax does not apply to sales of cold food products when sold on a “take out” or “to go” order.

Sales of carbonated beverages (such as soda or sparkling water) and alcoholic beverages are always taxable. In addition, sales of a combination package (two or more items sold together for a single price) are taxable if it includes any one of the following items:

- A hot prepared food (such as a hot sandwich or hot bakery item)
- A hot beverage (such as coffee or hot chocolate)
- A carbonated beverage
- An alcoholic beverage

Accordingly, sales of hot chocolate consumed at facilities provided by the retailer would be subject to tax. This is true regardless whether the purchase is of hot prepared food products or cold food products. Generally, if a business is located within a store and the store provides benches, tables and chairs in a general area, where customers of various sellers can consume food products, the area is considered the seller’s premises for tax purposes. To further explain, if the tables and chairs are located in close proximity to the seller and there is a reasonable connection between the food selling operations and the tables and chairs; or the seller must pay a fee to the store for the common food consumption area, this would constitute “facilities” within the meaning of Regulation 1603. However, consuming the hot chocolate while you are walking around the store shopping for other items does not constitute “facilities” provided by the retailer.

As such, assuming the Starbucks located inside the Target store does not meet both criteria of the 80/80 rule, your purchase of the hot chocolate on a to-go basis for a separate price is not subject to sales tax. The information you provided indicates that Starbucks likely collected excess tax reimbursement. Excess tax reimbursement would be the amount of sales tax collected on the hot chocolate.

Sales and Use Tax Regulation 1700, *Reimbursement for Sales Tax*, (copy enclosed), provides that when an amount represented by a person to a customer as constituting reimbursement for sales tax is computed upon an amount that is not taxable or is in excess of the taxable amount and is actually paid by the customer to the person, the amount so paid is excess tax reimbursement.

Whenever the board ascertains that a person has collected excess tax reimbursement, the person will be afforded an opportunity to refund the excess collections to the customers from whom they were collected. In the event of failure or refusal of the person to make such refunds, the board will make a determination against the person for the amount of the excess tax reimbursement collected and not previously paid to the state, plus applicable interest and penalty.

Based on the information presented in the article, it is not clear why sales tax was collected by Starbucks on the sale of the hot chocolate. The Board has an active audit program to ensure the correct application and remittance of sales and use tax by all taxpayers. Let me assure you that this agency does its best to verify that all taxpayers have accurately collected and remitted sales

and use taxes in accordance with the Sales and Use Tax Law. Accordingly, your article is being forwarded to our district office for review and/or investigation. However, because of confidentiality statutes we cannot provide you any information on the results of our efforts.

I would like to thank you for your interest in the proper administration of the California Sales and Use Tax program. I hope this information is helpful. If you have additional questions regarding this matter, or any other sales and use tax matter please write me again or call our Information Center at (800) 400-7115. You may also visit our website at www.boe.ca.gov.

Sincerely,

Anita Grandrath Gore, Deputy Director
External Affairs Department

AGG:jlg

Enclosures: Regulation 1503, *Hospitals and Other Medical Service Facilities, Institutions and Homes For the Care of Persons*
Regulation 1574, *Vending Machine Operators*
Regulation 1602, *Food Products*
Regulation 1603, *Taxable Sales of Food Products*
Regulation 1700, *Reimbursement for Sales Tax*
Publication 22, *Tax Tips for the Dining and Beverage Industry*

cc: Mr. Ramon J. Hirsig (MIC 73)

bc: Ms. Randie L. Henry (MIC 43)
Mr. Todd C. Gilman (MIC 70)
Ms. Freda Orendt (MIC 47)
Mr. Stephen R. Rudd (MIC 46)
Mr. Jeffrey L. McGuire (MIC 92)
Mr. Joseph D. Young (MIC 49)
Ms. Kelly Reilly (MIC 47)
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Mr. Henry Wong (CH)
Mr. James C. Kuhl, Sr. (MIC 44)
Ms. Trista Gonzalez (MIC 44)
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Ms. MaryAnn Hay (MIC 47)
Mr. Michael Loretta (MIC 46)
Mr. Larry Bergkamp (MIC 92)
Ms. Mariflor Jimenez (MIC 49)
Mr. Todd MacMurray (MIC 44)
Mr. Jose L. Gonzalez (MIC 44)
File – Complaints (MIC 44)